American Bankers Association

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CONSUMER BANKERS ASSOCIATION

October 18, 2016

Monica Jackson
Office of the Executive Secretary
Consumer Financial Protection Bureau
1700 G Street NW., Washington, DC 20552

Re: **Request for Comment on Proposed Amendments to Federal Mortgage Disclosure Requirements Under the Truth in Lending Act (Reg. Z), Docket No. CFPB–2016–0038**

Dear Ms. Jackson:

The American Bankers Association[1] and the Consumer Bankers Association[2] (the Associations) appreciate the opportunity to submit this comment in response to the Consumer Financial Protection Bureau's (Bureau or CFPB) request for comment on proposed revisions to the Federal mortgage disclosure requirements under the Real Estate Settlement Procedures Act and the Truth in Lending Act, as implemented in Regulation Z. (TILA-RESPA Integration Rule, *Know Before You Owe*, or KBYO).[3] The proposed rule sets forth multiple amendments to existing regulations and memorializes informal guidance and clarifications issued by the Bureau since the KBYO rule was finalized in December 2013.

The Associations appreciate the Bureau's attention to correcting, clarifying and technically amending provisions of the TILA-RESPA Integration Rule. Since the KBYO rule was issued, the Associations have communicated that these regulations raise significant implementation concerns as they are extremely complex and contain high-liability provisions that are often unclear and require official CFPB interpretation to appropriately resolve. We therefore commend the Bureau for responding to our top concerns, and appreciate the Bureau's current efforts to assist our industry in our ongoing compliance efforts.

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[1] The American Bankers Association (ABA) is the voice of the nation's $16 trillion banking industry, which is composed of small, regional and large banks that together employ more than 2 million people, safeguard $12 trillion in deposits and extend more than $8 trillion in loans.

[2] Founded in 1919, the Consumer Bankers Association (CBA) is the trade association for today's leaders in retail banking - banking services geared toward consumers and small businesses. The nation's largest financial institutions, as well as many regional banks, are CBA corporate members, collectively holding well over half of the industry's total assets. CBA's mission is to preserve and promote the retail banking industry as it strives to fulfill the financial needs of the American consumer and small business.

[3] Amendments to Federal Mortgage Disclosure Requirements Under the Truth in Lending Act (Regulation Z), 81 C.F.R. 54318 - 54387 (August 15, 2016)

Overview of Comments

The following list summarizes the Association's more important comments on the KBYO proposed changes:

1. CFPB should form an internal Task Force dedicated to mortgage regulatory matters that will engage with industry stakeholders to identify compliance and legal problems with KBYO (and other mortgage rules, as appropriate). Any issue identified by the group can be immediately analyzed and assessed in terms of the need for rulemaking and/or guidance publication.
2. CFPB should formally extended the current "Good Faith Compliance" examination policy until the end of the compliance deadlines for the current proposed rules.
3. Bankers continue to be affected by uncertainties regarding the liabilities under KBYO, and the Bureau should publish a description of specific statutory provisions relied upon to implement KBYO disclosures. In addition, the applicability of statutory cure provisions should be clarified.
4. The current status of the KBYO sample forms as model forms under TILA facilitates proper implementation and affords regulatory protection to lenders. The Bureau should retain the model form status of the sample forms and accord them binding safe harbor status.
5. The Associations support the Bureau's proposal to allow a creditor to use a corrected CD to reset applicable good faith tolerances when there are fewer than four business days remaining before consummation or when the Closing Disclosure has already been issued. This provision must be made applicable in instances involving fee changes due to interest rate variations.
6. The Bureau should clarify that fee corrections on the LE aimed at resetting the estimates for tolerance purposes must be provided on revised LEs, but that absent an intent to reset tolerances, all other appurtenant corrections are deemed "informational" and do not need to be continually updated on all revised LEs.
7. The Bureau should clarify that the disclosure advising on the date of expiration of estimated closing costs may be entirely removed from the LE disclosure after the customer's intent to proceed has been received by the bank. This ensures that blank spaces on the LE will not confuse consumers.
8. The Bureau should clarify the disclosure treatment of loan costs in Total of Payments where such costs are financed by the consumer.
9. CFPB should retain the current application of the 10% tolerance in instances where the creditor fails to provide a written list of providers.
10. With respect to construction financing (and other loans with respect to payoffs generally), the Bureau should avoid consumer confusion by requiring the disclosure of payoffs and construction costs as payoffs in Summaries of Transactions, and in the Adjustments and Other Credits row of the "calculating-cash-to-close" table. In addition, the Bureau should not require the provision of a permanent loan LE when the consumer applies only for a construction-only loan. More importantly, given the nature and variations inherent in construction lending, the Bureau should exclude construction loans from KBYO coverage altogether.

<u>General Comments</u>

Prolong Policy of Examinations Based On "Good Faith Compliance"

As you are aware, the banking industry is currently operating under a temporary bank examination phase that acknowledges the difficulties inherent in current regulations and recognizes bank efforts to comply in good faith with the KBYO requirements. Our members appreciate this narrowly tailored policy that allows needed flexibility, and we request that this examination approach be formally extended until the end of the compliance deadlines for the current proposed rules. We urge that the Bureau recognize that there will be a period of time following implementation when mortgage lenders may make inadvertent errors, notwithstanding their best efforts to comply. There are real difficulties in compliance with this massive and complex new regulatory regime, and there is no way to "soft launch" these changes or test them in a real world environment. Once the changes go live they will have to be perfect for every consumer transaction on day one. We suggest that our request to extend the current "good faith compliance" policy is a fair and practical approach to facilitating a smooth transition into the new regulations.

We note that anything short of this would be senseless and even disruptive to current mortgage operations. Most institutions—particularly smaller banks—are still struggling with KBYO implementation issues, and many are still bringing their systems up to par with the new requirements—some that were announced verbally and only recently codified (on October 12, 2016) in the "*Know Before You Owe Small Entity Compliance Guide*." The rules advanced under this proposal will again alter the regulatory landscape under KBYO and force tweaks and changes to our compliance and loan origination systems. It would be pointless to remove the current diagnostic examination policy and revert to a strict enforcement stance precisely when banker systems are going to be advancing with changes required by this rulemaking. As we describe in detail below, many of the changes being proposed here will impact banker systems and require changes to interconnected LOS functions.

In short, to assure that these rule transitions are well implemented, the current good faith compliance period should be made coextensive with the implementation period afforded under this new rule.

Need to Clarify Liabilities

A most critical element of uncertainty under KBYO continues to be the scope and effect of RESPA and TILA's liability provisions given the integration of the two sets of disclosures. Since the launch of the KBYO reform implementation process, banks have expressed significant anxiety about which statutes' remedies are effective under particular circumstances and the extent to which they affect non-creditors, including settlement agents and investors. The continued uncertainty in liability forces industry stakeholders to assume that the more stringent liability will apply in all instances of non-compliance, even if that is not the intent of the law or the Bureau. In the long run, the resulting impact to consumers is grim—lenders and investors will avoid exposure to uncertainty and confusion, and this will result in diminished product choice and increased costs for borrowers.

The Associations have consistently called for more transparency regarding risks that stem from unintentional mistakes and technical non-compliance with the KBYO rules. The complexity of the regulations, the intricacy of the KBYO disclosure forms, and the infinite number of scenarios involved in mortgage finance create a situation where inadvertent mistakes or instances of non-compliance are unavoidable. In addition, there are differences in the interpretation of various provisions under KBYO between lenders and investors, which are easily resolved by clarity in how KBYO liabilities apply. In short, it is the CFPB's responsibility as a policy maker to affirm with certainty what law they are relying on for the different provisions. That is good public policy. It will also result in more consistent outcomes for consumers when courts interpret the law, and, most importantly, it is a critical piece of information for compliance so banks know what cure provisions apply.

The Associations recommend that the Bureau provide a more detailed description of the specific statutory provisions under RESPA and/or TILA (or other statutes) it relied upon for each provision of the KBYO disclosure provisions contained in the December 2013 final rule. The Associations believe that it is only though a more precise description of the statutory authority for each disclosure element that industry stakeholders and government authorities will be able to properly identify penalties and liabilities applicable under the law. We have submitted, in past communications, recommendations for sample documents containing a bright-line matrix of all the various disclosure elements of the Loan Estimate and Closing Disclosure forms (i.e., the Projected Payments table; Estimated Taxes, Insurance & Assessments table; AIR/AP table, others). Under such a matrix, the Bureau could explicitly address how liability might attach to any specific error. Any such matrix should include: (1) each regulatory provision that provides for a disclosure item or requirement; (2) a description of the statutory section relied upon for each disclosure item or requirement; (3) if curable, how it may be cured, e.g., as a tolerance refund, as a non-numeric clerical error, or under Section 130(b) of TILA; and (4) any comments.

We understand that developing such a matrix would require that the Bureau issue additional clarifications beyond the items defined by the present proposed rulemaking. Nonetheless, we think this additional effort would be of considerable value, as stakeholders urgently need this guidance, and consumer interests would be greatly enhanced by the added clarity. Although the CFPB informally issued a blank Loan Estimate and Closing Disclosure that annotated the disclosure with the statutory sections under Part B of TILA that were "referenced" in the preamble, these annotated disclosures are of limited usefulness because they are informal, do not specifically address individual disclosure items, and for some provisions may conflict with the preamble of the 2013 final rule with respect to the statutory authority relied on or implemented. If the Bureau provided a matrix as described herein, issued via official commentary to the regulations, it would facilitate proper application of the law, and would allow market participants to recognize and manage their responsibility and/or accountability in the transaction.

Cure Provisions

The cure provisions under KBYO are extremely limited. Only two cure provisions exist: one for tolerance violations and the other for non-numeric clerical errors. This means that there is no provision for lenders to fix other inadvertent mistakes that may not actually harm a borrower. The preamble of the 2013 final rule acknowledges that lenders can use the cure provisions under TILA. Current TILA sets forth two provisions for lenders and investors to limit liability for certain errors. These provisions state that creditors or their assignees can—

> (1) Avoid liability under TILA for "any failure to comply with any requirement imposed under [Part B]" if the creditor or assignee: (a) notifies the consumer of the error within 60 days of discovery (but before an action has been instituted or the borrower notifies the creditor of the error in writing); and (b) "makes whatever adjustments in the appropriate account are necessary to assure that the person will not be required to pay an amount in excess of the charge actually disclosed, or the dollar equivalent of the annual percentage rate actually disclosed, whichever is lower." (15 U.S.C. § 1640(b)); and
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> (2) Avoid civil liability or an extended right to rescind under TILA "if the creditor or assignee shows by a preponderance of evidence that the violation was not intentional and resulted from a bona fide error notwithstanding the maintenance of procedures reasonably adapted to avoid any such error. Examples of a bona fide error include, but are not limited to, clerical, calculation, computer malfunction and programing, and printing errors, except that an error of legal judgment with respect to a person's obligations under this subchapter is not a bona fide error." (15 U.S.C. § 1640(c))

The application of these statutory cure provisions, especially TILA section 130(b), to KBYO is unclear, because they historically have not applied to the substantial amount of information that must be disclosed under KBYO. For this reason, there are many different interpretations in the industry regarding the applicability of these statutory cure provisions.

In a December 29, 2015 letter to the financial industry, Director Cordray added interpretive details to these cure provisions by stating that, "consistent with existing [TILA] principles, liability for statutory and class action damages would be assessed with reference to the final closing disclosure issued, not to the loan estimate, meaning that a corrected closing disclosure could, in many cases, forestall any such private liability." We read this statement to mean that CFPB believes that many TILA violations on the Loan Estimate or Closing Disclosure may be "cured" with a corrected final closing disclosure. It would be useful if the Bureau formalized this interpretation via incorporation of this language into KBYO's regulatory text or commentary. The Associations request that this be done in any final rule.

Model Forms

The Associations are concerned with the Bureau's statement in the proposed rule preamble that the "integrated disclosure samples, unlike the integrated disclosure model forms, are not controlling authority for any purpose." The Bureau goes further to assert that "they should not be read as changing or overriding the requirements…," and that sample forms "are provided by the Bureau purely for illustration and as an aid to compliance. Because any errors in the integrated disclosure samples have such limited legal consequences, the Bureau has not conducted a systematic review of their accuracy; should the Bureau undertake such a review in the future and identify errors, it will adopt appropriate revisions." The Bureau also proposed to amend comment app. H-30 to remove references to the sample forms as model forms under TILA.

The Associations appreciate that the sample forms are meant to be illustrative of much of the dynamic text that does not appear on the blank forms, such as the bullets in the Loan Terms and Calculating Cash-to-Close tables. As mentioned elsewhere in these comments, the KBYO disclosure rules are enormously complex and often attempt to provide textual descriptions of mathematical calculations. In many instances, these descriptions are only comprehensible when accompanied by actual examples that set forth mathematical calculations of hypothetical transactions. For that reason, many banks have utilized the sample forms to discern substantive requirements under the rule, such as the placement of fees, the calculation of In 5 Years and the Total of Payments, the calculations in the Escrow Account disclosure on page 4 of the CD, and the rounding requirements. The Bureau's use of these sample completed forms is extremely valuable to banks, and we see no reason to strip them of safe harbor for compliance or their standard form status. Using these forms as roadmaps to assure compliance serves to improve implementation and ensure consumers receive the disclosures in the format that the CFPB intended. Importantly, the dynamic text of the form cannot be modified to the detriment of consumers in any way.

In addition, the industry, based on the plain language of the regulatory text of §§ 1026.37(o)(3) and 1026.38(t)(3), comment app. H-30, and the preamble of the 2013 final rule, has interpreted the sample forms to have the status of model and standard forms under TILA and RESPA. Sections 1026.37(o)(3) and 1026.38(t)(3) refer to forms H-24 and H-25 as model forms, which references do not differentiate between blank or sample forms and appear to have been intended to be inclusive of the sample forms. It appears that the Bureau intended that the sample forms have the status of model forms and standard forms under TILA and RESPA, because the preamble of the 2013 final rule states the following:

> Forms H–24(A) and (G), and forms H–25(A), and (H) through (J) are blank forms. The other forms under H-24 and H-25 illustrate the disclosures required under §§ 1026.37 and 1026.38, for particular types of transactions. For federally related mortgage loans, the disclosures under §§ 1026.37 and 1026.38 are required to be made as illustrated by such forms, including their formatting (e.g., using bold font where illustrated). The Bureau has added comment app. H-30 to add clarity regarding this issue.

We urge that these forms currently have, and should continue to be accorded, binding authority as both model forms under TILA and standard forms under RESPA for loans subject to KBYO. Instead of eliminating the model or standard form authority of these sample forms, the Bureau should actively work to review these forms to eliminate any inconsistencies or errors, to ensure the forms illustrate the Bureau's intended format for the disclosures.

The Associations respectfully request that CFPB reconsider its statement that sample forms "are not controlling authority for any purpose" and its proposed amendment to comment app. H-30. To the contrary, the Associations would ask that the Bureau clearly acknowledge the current status of the sample forms in the final rule and clarify that creditors can use them to guide their formatting and calculations for the disclosures. This would assist the industry, including creditors, investors, settlement agents, and technology vendors in ensuring compliance and that the disclosures are provided as the CFPB intended.

Eliminate Retroactive Liability

Members of the Associations are very appreciative of the numerous amendments offered in this proposal, and our preliminary analysis reflects that this proposed rule will resolve multiple ambiguities that banks deem significant. We hope the Bureau understands that many of the ambiguities corrected in this second KBYO rulemaking had to be previously resolved by banks via interpretive assumptions that will now be rendered erroneous due to these proposed clarifying amendments. We note that the CFPB has already acknowledged that there has been confusion surrounding some requirements in the rule, such as the Total of Payments.

Banks and legal experts have expressed concerns that it is unclear, in most cases, whether the Bureau intends these proposed amendments that provide for tolerances to apply only prospectively, or that the clarifications indicate that alternative interpretations were incorrect under the current rule. In addition, because the proposed amendments would not alter the provisions for "curing" errors, it is uncertain whether liability concerns will remain for loans originated prior to the effective date of the amendments.

The Associations would urge that the Bureau explicitly allow that any tolerance or cure provisions enacted in this rulemaking be made available for loans that predate this proposal. This step would allow for the correction of previous non-compliance caused by the interpretive ambiguity that the Bureau is now fixing.

Second, the Associations would ask that, in any preamble issued with the final rule, the CFPB articulate the problems that led the Bureau to enact the change or clarification. Such articulations, even if brief, would go a long way in allowing institutions to defend themselves in instances where they are unfairly targeted for legal action for merely attempting to comply with the law. Finally, the Bureau should, for the requirements for which the Bureau acknowledged confusion, also describe in the preamble of the final rule that interpretations it believes are reasonable under the current rule.

Periodic Updates to Regulations

The Associations believe that proper administration of the mortgage disclosure laws require continuous rule upgrades and ongoing attention to implementation details. The reality of the new regulatory environment imposed by the Dodd Frank Act reforms and the integrated disclosure rules is that regulatory technicalities will govern mortgage transactions very tightly. The new disclosure regime is extremely prescriptive—KBYO provides very specific regulations that delineate how every cost must be calculated, reflected in the forms and apportioned in mandated comparison tables. Any variance in any aspect of a covered transaction must now be accommodated in accordance with detailed disclosure procedures.

While this level of detail may in some ways facilitate compliance, it also means the regulation must be monitored to ensure it provides sufficient and appropriate rules for the evolving regulatory and business landscape.

At the same time, there is also a constant state of evolution in the market and in the financial world that our banks must continuously contend with. Note the following observations regarding the current housing finance environment generally—

- Home finance products are extremely dynamic and change with time;
- Mortgage products are tailored to serve specific communities and specific purposes;
- Automation and new technologies (e.g., smartphones) are changing the market landscape and mutating consumer expectations;
- Legislative reforms have considerably changed the regulatory infrastructure of mortgage lending in a relatively short amount of time;
- Investor requirements continue to evolve and secondary market demands are shifting.

These points reflect that there is constant change and development in our mortgage markets and our approaches to mortgage finance. In order to accommodate shifts and advances, banks require a regulatory system that is fast and efficient in responding to change.

The Associations believe that, moving forward, the Bureau should provide regular, periodic, and authoritative formal guidance regarding the application, scope, requirements, and liabilities of KBYO. This could be done through regular amendments to the Commentary or the Regulation, following notice and comment, to address issues that have arisen. To this end, the Associations request that the CFPB form an internal Task Force dedicated to mortgage regulatory matters that will engage with industry stakeholders to identify compliance and legal problems with KBYO (and other mortgage rules, as appropriate). Any issue identified by the group can be immediately analyzed and assessed in terms of rulemaking and/or guidance publication. This task force will assure that there is keen focus on housing finance issues and early attention on regulatory matters, as they arise. Under this approach, compliance uncertainties and issues will be identified swiftly, policy and operational issues will be analyzed with input from industry stakeholders, and these issues will be properly and appropriately addressed. The shared goal is to create a system that quickly and effectively addresses compliance problems so that mortgage lending can continue to evolve to provide consumers with financing for homeownership that best serves their needs into the next decade, and beyond.

Comments on Specific Proposed Provisions

"Black Hole" Solution

The Associations appreciate the Bureau's attention to resolving problems involving instances where delays caused by events outside the control of the lender force unnecessary, but often consequential, delays and postponements in settlements. The existing rule and commentary are very ambiguous with regard to the ability to update fee revisions for tolerance purposes (*i.e.*, the good faith analysis under § 1026.19(e)(3)) after delivery of a CD. The Associations have raised concerns about the "black hole" effect in these regulations, and our worries have consistently focused on two related prongs—ensuring maximum consumer benefit and flexibility, and eliminating substantial and unwarranted liability and cost for banks.

In this sense, the Associations are very pleased that the Bureau is proposing such a simple and uncomplicated solution to this vexing problem. As described by the proposed rule's preamble, the Bureau proposes to allow a creditor to use a corrected CD to reset applicable good faith tolerances when there are fewer than four business days remaining before consummation or when the Closing Disclosure has already been issued, provided that the creditor also complies with the other requirements of § 1026.19(e)(4).

The Bureau is proposing to add comment 19(e)(4)(ii)-2 to clarify this point, which would state—

> "If there are fewer than 4 business days between the time the revised version of the disclosures is required to be provided under § 1026.19(e)(4)(i) and consummation or the Closing Disclosure required by § 1026.19(f)(1) has already been provided to the consumer, creditors comply with the requirements of § 1026.19(e)(4) (to provide a revised estimate under § 1026.19(e)(3)(iv) for the purpose of determining good faith under § 1026.19(e)(3)(i) and (ii)) if the revised disclosures are reflected in the corrected

> disclosures provided under § 1026.19(f)(2)(i) or (2)(ii), subject to the other requirements of § 1026.19(e)(4)(i)."

We interpret this language to mean that after an initial CD has been provided to the consumer and there is a subsequent valid changed circumstance (or customer requested change), the creditor would be allowed to provide the customer with a revised CD that would reset the tolerances. The only stipulation to the creditor's ability to reset tolerance is that the revised CD must be delivered to the consumer within 3 business days of receiving information sufficient to establish a valid changed circumstance. If this articulation is reflective of the intended application of the proposed rule, the Associations would commend the change as a prudent and very effectual resolution to this difficult problem. The use of corrected CDs as a vehicle for correcting and "re-baselining" fee disclosures is a straightforward approach to returning regulatory order and compliance clarity on this provision.

We urge, however, additional attention with regard to the following points—

- *CD at Closing*: CFPB should consider clarifying the time period in which a revised CD must be provided after the creditor receives information sufficient to establish a change justified by the rule's "changed circumstances" or "borrower requested change" provisions. It appears from the proposal that proposed comment 19(e)(4)(ii)-2 would require the creditor to provide a revised CD within 3 business days of learning of such a reason for a revised estimate, because of the comment's reference to the revised CD being provided, "subject to the other requirements of § 1026.19(e)(4)(i)." However, § 1026.19(e)(4)(i) does not provide for any requirements that are applicable to a revised CD provided pursuant to § 1026.19(f)(2)(i) or (ii). For this reason, the effect of this reference is unclear. While the 3-day deadline for providing a revised Loan Estimate under § 1026.19(e)(4)(i) may be appropriate for a revised CD in some situations when closing is delayed greater than 3 business days, in many situations a change occurs when closing is scheduled to occur less than 3 business days after the change. In this situation, we believe the CFPB should clarify that the revised CD can be provided at the closing table, and can reset tolerances, if the closing occurs <u>prior to</u> the end of the 3-business-day period after establishing the changed circumstance.

  We do not believe such a clarification would lead to consumer harm. Without such a clarification, some banks may delay closing to ensure they can provide such a revised CD before the day of closing, which may negatively impact consumers that need to meet certain deadlines. To illustrate this point, the Bureau should add the following example: If a closing were delayed by 2 days, the revised CD could be provided at closing. If it was delayed 5 days, the CD would have to be provided to the consumer within 3 business days of establishing the changed circumstance or borrower requested changes. And the example could clarify that in both instances, the revisions could be used to "re-baseline" the changed fees.

- *CD at Closing*: Further, the CFPB should clarify that a revised CD could be provided for tolerance purposes pursuant to proposed comment 19(e)(4)(ii)-2 at the conclusion of settlement. We note that under the current rule, the good faith analysis takes into account the actual costs paid by or imposed on the consumer at the later of consummation or settlement, pursuant to comment 19(e)(3)(i)-2. Many legitimate, justified changes based on "changed circumstances" or borrower requested changes can occur at settlement, when settlement occurs after consummation of the transaction, and a creditor should not be forced to absorb the costs of such legitimate changes.

- *Interest Rate Dependent Charges*: There is lingering uncertainty as to whether the solution defined in proposed comment 19(e)(4)(ii)-2 would apply in instances concerning fee changes due to interest rate changes. The Associations believe there must be added clarity regarding whether the proposed solutions herein would also apply to interest rate dependent charges that change due to a rate lock that occurs after a Closing Disclosure is provided. According to the preamble, the Bureau is proposing a new comment to 19(e)(3)(iv)(D)-2 that would address "Interest Rate Dependent Charges" by stating that— "*If the interest rate is locked on or after the date on which the creditor provides the Closing Disclosure and the Closing Disclosure is inaccurate as a result, then the creditor must provide the consumer a corrected Closing Disclosure, at or before consummation, reflecting any changed terms.*"

  The Associations concur with this phrasing, but believe that it is very important that this provision be made consistent with the determinations set forth in proposed comment 19(e)(4)(ii)-2, above. This provision must therefore explicitly incorporate a statement that any revised CD delivered pursuant to interest rate changes will reset tolerances based on § 1026.19(e)(3)(iv)(D). Absent this additional language, fee variations associated with interest rate changes (often beneficial to the consumer) will remain subject to the "Black Hole" problem. This is also important because § 1026.19(e)(3)(iv)(D) is the only reason for revising estimates for tolerance purposes that expressly allows changes to lender credits, which often do change when a borrower locks in an interest rate. This can occur when a borrower who has been letting the interest rate float throughout the origination process decided to lock in an interest rate, or a borrower has decided to float down a locked interest rate after the initial CD has been provided.

  An additional change that the CFPB should make to clarify the treatment of tolerance resets for interest rate dependent charges involves moving the "interest rate dependent charges" provision to the changed circumstances provision. Specifically, the Associations recommend that there be an amendment to § 1026.19(e)(3)(iv)(A), the section that describes valid "changed circumstances," to incorporate subsection (D) into that list. This would result in explicitly including the locking of an interest rate's effect on "interest rate dependent charges" as a "changed circumstance," which would provide the needed clarification of using rate locks as a reason for revision on the CD, as described above.

Revised Loan Estimates and Informational Loan Estimates

The Associations appreciate the Bureau's focus on the rule's "lingering uncertainty" as to whether a creditor is prohibited from providing the consumer with a revised Loan Estimate for informational purposes (generally occurring when a revision is not based on any of the valid reasons for revision of estimates defined in §1026.19(e)(3)(iv)(A) through (F)). Banks agree with the solution set forth in the proposal that would add a new comment to explicitly clarify that the rule does not prohibit the creditor from issuing revised disclosures for informational purposes only, even outside the scope of valid changed circumstances. The Associations also agree that the provision of these informational re-disclosures is entirely optional under the rule.

The Associations have concerns, however, that the Bureau goes further and advances with an additional mandate on LE revisions in instances of LE revisions aimed at resetting tolerances. In the preamble, the Bureau states that regardless of whether a creditor issues a revised Loan Estimate *to reset tolerances* or simply for informational purposes, any disclosures on the revised Loan Estimate must be based on the best information reasonably available to the creditor at the time the disclosure is provided to the consumer. The commentary goes on to clarify, via an example, that "any increases in those other charges unrelated to the lock extension may not be used for the purposes of determining good faith under § 1026.19(e)(3)."

In short, the Bureau is stating that where a lender issues a revision to an LE to re-baseline fees for purposes of tolerance comparisons, it <u>must</u> also accurately update all other fee changes in order to be deemed "in good faith."

The Associations understand the Bureau's concern that every LE, including revisions, must list fees disclosed in good faith and based on best information reasonably available to the lender. However, the Bureau is setting forth a mandate that is extremely complex from a systems perspective. To comply with the proposal, a lender would have to possess re-disclosure systems that detect 3 variant types of fee corrections: one that recognizes a fee correction that resets the tolerance baseline, one that that recognizes a fee correction for informational purposes only, and yet another that recognizes a fee correction that does not reset a tolerance baseline, but that must still be flagged as a change that could count as a reset if there are eventual fee increases that could eventually trigger the 10% tolerance threshold. The multidimensional detection system that the Bureau is mandating via these instructions is very sophisticated and not currently part of existing LOS frameworks. The reconfigurations required to achieve accuracy in a system that contains all these detection layers will entail very significant systems upgrades and reconfigurations. In the short-term, this new mandate will require manual work-arounds that will threaten compliance and risk secondary market rejection.

To alleviate such high burdens on banks, the Associations recommend that the Bureau clarify that fee corrections on the LE aimed at resetting the estimates for tolerance purposes must be done in good faith, but that absent an intent to reset tolerances, all other appurtenant corrections are deemed "informational." Stated differently, a revised LE that resets tolerances would have to list the fee changes that "re-baseline" the tolerance under a strict "good faith" standard, but the updated LE need not list every other incremental fee variance as a mandated component of the revised LE. The Bureau should clarify that non-tolerance items on re-disclosures remain strictly optional.

The Associations do not believe that this approach threatens consumer interests. Small and marginal fee differences cannot be deemed material to a consumer so long as they remain strictly within established tolerance levels. In addition, many of the costs on the LE are not subject to specific tolerance percentages, and the creditor would not be required to provide any revised LE for changes in such costs absent the provision of a revised LE for tolerance purposes as proposed. It appears from this aspect of the rule that the CFPB does not believe consumers would be harmed by learning of “informational” changes in such costs on the initial CD when a revised LE is not provided for other purposes. Overall, it does not appear that this proposal addresses an injury that the Bureau deems in any way significant, although it would represent a significant operational burden on the industry.

In the long-term, we believe that vendors will work to refine systems so that even minute changes will be appropriately classified and tabulated thus making all revised LEs accurate to the cent. Once these systems are tested as precise and workable, lenders will ensure that that they are incorporated appropriately. In the short-term, however, retaining an optional standard towards all informational LEs and non-tolerance LE corrections will avoid sudden and unworkable (perhaps impossible) system overhauls.

Closing Cost Expiration

The Bureau is proposing to resolve uncertainties regarding whether a creditor can reset tolerances where the consumer indicates an intent to proceed after the 10-business-day period, but within a longer period for which the creditor promised to honor the estimated charges originally disclosed on the Loan Estimate. The Associations support the Bureau’s proposed solution, to be set forth in a new comment 19(e)(3)(iv)(E)-2, that where a creditor voluntarily extends the consumer acceptance period to a period greater than 10 business days, that longer time period becomes the relevant time period for purposes of using and delivering the revised estimates under § 1026.19(e)(3)(iv)(E). Furthermore, the Associations generally support the proposal to add comment 37(a)(13)-4 that would provide that, once the borrower has indicated an intent to proceed, the expiration date must be left blank on subsequent Loan Estimates. The Associations offer two comments on these solutions:

- *Consumer Confusion*: The Associations recommend that subsequent LEs should be allowed to entirely omit the sentence on the current form that advises the consumer about the expiration date. Banks are concerned about negative consequences from leaving blank spaces in official disclosure forms. If the advisory language remains on the LE form but is just left blank, the consumer will be able to see the language that warns about the expiration of the estimates. This is certain to cause consumer alarm, because they may believe the estimates on revised LEs are also subject to an expiration date. Significantly, the CFPB has not tested its proposed method of disclosure under proposed comment 37(a)(13)-4 with consumers in any qualitative or quantitative consumer testing. The CFPB cannot know how consumers will interact with this blank space on the disclosures without sufficient consumer testing, and thus, should carefully consider the potential confusion caused by its proposed method of disclosure that would leave an important section of the disclosure blank. In addition, and more delicately for banks, a blank space on a formal document will likely lead to customer suspicions that the financial institution is hiding or obfuscating an important date. In either scenario, the relationship with the consumer would be affected negatively. The Associations recommend that the Bureau clarify that the sentence advising that “All other estimated closing costs expire on ____” be entirely removed from the LE disclosure after the customer's intent to proceed has been received by the bank, to ensure a blank space will not cause confusion for consumers.

- *Implementation Period:* The Associations note that the disclosure that the Bureau is proposing to amend here is currently one that is hard-coded into bank compliance systems and forms software. A change that requires the use of a blank space (or, as suggested, the deletion of a sentence from the form) would create the need to alter bank disclosure software. We, therefore, recommend that the CFPB provide sufficient time for industry to implement this programming change to their systems, and test its use to ensure it is only triggered at the appropriate time. This implementation period will go a long way in alleviating vendor costs and accommodating banks that will be stressed in their ongoing mortgage regulatory implementation obligations.

Total of Payments Disclosure

- *Tolerances:*

The TILA-RESPA Final Rule requires the disclose of the total of payments on the Closing Disclosure as the sum of principal, interest, mortgage insurance, and loan costs. The proposed rule would add a new tolerance for the total of payments, and also seeks to clarify which "loan costs" are included in the calculation.

The Associations appreciate the Bureau's attention to this disclosure item, as the total of payments is one of the disclosures with civil liability implications as set forth in TILA section 130, including actual damages, statutory damages (individual and class action), costs, and attorney's fees. Specifically, the proposal would revise § 1026.38(o)(1) to provide that the disclosed total of payments shall be treated as accurate if the amount disclosed: (i) is understated by no more than $100 or (ii) is greater than the amount required to be disclosed. The Bureau would explain, via comment 38(o)(1)-1, that the total of payments is calculated in the same manner as the "In 5 Years" disclosure under § 1026.37(l)(1)(i), except that the disclosed amount reflects the total payments through the end of the loan term.

The Associations have no further comments on this proposed item. We agree with the addition of a tolerance for total of payments that mirrors the existing tolerances for finance charges but that apply independently from the finance charge itself—i.e., it is not affected by whether the Finance Charge in that transaction was disclosed accurately or not. The Associations believe that the approach proposed by the Bureau will positively impact secondary market execution by affording investors comfort that minor inaccuracies do not raise liability concerns.

- *Calculation:*

Another important proposal in this section would revise comment 38(o)(1)-1 to clarify that the total of payments calculation on the Closing Disclosure excludes charges for loan costs disclosed under § 1026.38(f) that are designated on the Closing Disclosure as paid by seller or paid by others. As explained by the preamble, a seller or other party, such as a lender, may agree to offset a particular loan cost, whether in whole or in part, through a specific credit, for example, through a specific seller or lender credit. The proposed revision to the comment would clarify that because these loan costs are not paid by the consumer, the amounts of such loan costs offset by specific credits are excluded from the total of payments calculation.

The Associations agree with this proposal but would request further clarification. The clarifications to only include borrower-paid loan costs in the total of payments would benefit from additional explanations about whether the following costs are included in the total of payments—

- *Instances where loan costs are financed*: In instances where the consumer chooses to lower closing or other costs by financing such costs through the loan, the borrower is technically paying for the fee (by adding it to the principal amount or obtaining a premium interest rate, thereby paying additional interest). However, because the payment of the fee is added to the principal amount or the interest rate, it would be double counted if it also had to be added to the total of payments as a loan cost. The CFPB should clarify whether such financed loan costs are included in the total of payments as loan costs, or should be excluded because they are financed.
- *General vs. Specific Lender Credits:* There is still considerable confusion regarding the distinction between general and specific lender credits, and whether general lender credits can be excluded from total of payments, or whether only specific lender credits may be excluded. Many banks use disclose lender credits as general lender credits instead of specific lender credits, in part, because they believe it is clearer and easier for the consumer to understand. The CFPB should clarify whether general lender credits can be subtracted from the total of payments.
- *Discussion of Uncertainty:* Since the issuance of the KBYO final rule, creditors have had significant difficulties in determining what loan costs must be included in the total of payments calculation. As such, and consistent with our comments above, it would be of great benefit if the Bureau would take the opportunity, in the preamble to the final rule, to discuss the rule's uncertainty in this respect, and offer that the current fixes are meant to impose clarity that did not exist before. This would go a long way in allowing lenders with previous difficulties to protect themselves against perceived violations when undertaking bona fide, "good faith" attempts to comply rather than engaging in purposeful misapplications of the law. As the CFPB's Director, Cordray, has stated on a number of occasions, the CFPB's supervision with respect to the rule would be sensitive to an institution's good faith efforts to implement and comply with the rule. It would be beneficial if the CFPB acknowledged the considerable confusion with respect to this calculation, and that incorrect methodologies for this calculation do not necessarily indicate a failure to undertake a good faith effort to comply with the rule. Further, it would be beneficial if the CFPB acknowledged that alternative interpretations of the total of payments, such as an interpretation that all loan costs paid by any party are included in the total of payments calculation, may be considered reasonable under the current version of the rule.

Cash-to-Close Calculations

The Associations appreciate the Bureau's attention to the "calculating-cash-to-close" table. The table is designed to maximize consumer understanding and offer a "reasonably reliable estimate of the cash due from or to the consumer at consummation." The Associations believe the calculating cash-to- close table provides a benefit to consumers. The table enables consumers to understand the components of their "cash-to-close," without the need to delve into the many details of the Summaries of Transactions. However, in spite of this important benefit to consumers, the industry has experienced some difficulties in completing the table in certain situations according to the current regulation.

The CFPB proposes multiple changes to the "calculating-cash-to-close table" for the LE and CD. A most important proposal deals with the handling of "cash-out" deals. More specifically, section § 1026.37(h)(1)(iii)(A) currently requires that disclosure of the down payment amount in a purchase transaction appear as a positive number. Comment 37(h)(1)(iii)-1 explains that, in the case of a transaction (other than construction loan) where the loan amount exceeds the purchase price of the property, the amount of the down payment disclosed must be $0. The Associations have, in past occasions, alerted the CFPB that this result is untenable, as loan funds that are remaining after the payment of obligations cannot be applied anywhere else in the table, and therefore, the "cash-to-close" figure ends up incorrect.

The Associations support the solution set forth in the proposal. As we understand it, the Bureau proposes a specific revision to § 1026.37(h)(1)(iii)(A) to account for amounts disbursed to the consumer (or used at consumer's discretion at consummation). Under Revised § 1026.37(h)(1)(iii)(A)(1), the rule would specify that, in a purchase transaction, the creditor subtracts the sum of the loan amount from the sale price of the property. Revised § 1026.37(h)(1)(iii)(A)(2) would provide that, in a purchase transaction, when the sum of the loan amount (and any amount for loans assumed or taken subject to that will be disclosed on the Closing Disclosure) exceeds the sale price of the property, the creditor calculates the estimated funds from the consumer in accordance with proposed § 1026.37(h)(1)(v), as revised. The CFPB proposed analogous revisions to the sections applicable to the CD.

Stated differently, under the Bureau's fix, where a down payment turns out to be negative due to cash back derived from a higher loan amount, the lender would use the provisions pursuant to "Funds for Borrower" at § 1026.37(h)(1)(v) (and the analogous section for the CD), which is the calculation applicable to refinance transactions that currently deals with funds remaining after the consumer pays all obligations.

The Associations support these proposed revisions. A clear confirmation of this interpretation would be of value.

Written List of Providers

The Bureau is proposing to clarify that a failure to provide a written list of providers results in 0% tolerance on that charge. The rule would set this forth via amendments to comments 19(e)(3)(ii)-2 and 19(e)(3)(iii)-2. In the preamble language, CFPB states "the Bureau believes that a creditor did not permit a consumer to shop if the creditor failed to provide a written list of providers in compliance with § 1026.19(e)(1)(vi)."

The Associations are concerned with this provision as they raise uncertainty regarding the regulatory repercussions of other situations involving mistakes or omissions involving the written list. First, it is unclear how the new regulation would treat an instance where a fee is mistakenly omitted from the list. Although the Bureau provides some language that where a creditor omits a fee, they can still collect it. This ability to collect a missing fee is not at all clear from current regulatory language. The proposed comments state that noncompliance with the requirements applicable to the written list of providers would also trigger the 0% tolerance. The application of a 0% tolerance in these instances means that minor mistakes on a written list of providers are incurable, and there is realistically no ability to fix an inadvertent omission at all.

The problem for lenders is exacerbated because the rules do not provide any mechanism for updating the written list of providers. The Bureau, via informal webinars, has stated verbally that lenders can update the written list of providers, but that this must be done with a new LE. This informal oral advisory is missing from the current proposal. Thus, it appears from the regulatory text that new fees added to the “shop for” category after provision of the initial LE and the original written list of providers would not be able to be disclosed on a new or revised written list of providers. For this reason, plaintiffs may look to the plain language of the rule and claim violations of the tolerance requirements in cases where creditors simply added fees to the “shop for” category because of changed circumstances.

The Associations suggest that the CFPB should retain the current treatment of charges under the tolerances when the creditor fails to provide a written list of providers under current comment 19(e)(3)(iii)-2. This proposed amendment would not provide “greater certainty and clarity,” which is the purpose the CFPB stated for the proposed rule.[4] Although the CFPB stated in informal guidance during one of its webinars that the failure to provide the written list of providers causes charges to fall into the 0% tolerance category, such informal guidance conflicted with the current comment 19(e)(3)(iii)-2. Under this current comment, when the creditor fails to provide the written list of providers, charges for which the consumer shopped for a provider and selected a provider not identified on the written list of providers fall into the category of charges subject to a 10% tolerance under § 1026.19(e)(3)(ii). This is the approach that the industry has implemented, following the plain language of the rule and commentary. The CFPB’s proposed amendment would represent a completely new tolerance rule that the industry would be required to implement, requiring substantial systems updates, testing, and staff training.

We also believe that the current approach under comment 19(e)(3)(iii)-2 is reasonable, and as described below, has been the framework for the tolerances and written list of providers since the Department of Housing and Urban Development (HUD) promulgated the current version of Regulation X, effective in 2010. If charges for which the consumer could shop for the provider were placed into the 0% category as a result of the failure of the creditor to provide the written list of providers, or fully comply with the requirements for the list, the creditor would be held to a standard of 100% accuracy for the costs of unaffiliated third parties over which they have no control and do not require the consumer to use. Under this result, creditors would be forced to absorb many increases in costs that may be due to valid changed circumstances or borrower requested changes. For example, creditors would be forced to absorb the cost increases of unaffiliated title companies, surveyors, pest inspectors, etc. This would include increases due to the consumer’s decision to purchase additional services, such as enhanced insurance policies or

[4] 81 Fed. Reg. at 54320.

inspections. In addition, this proposal may provide an incentive to service providers to increase their prices upon learning of the creditor's failure to provide a fully compliant written list of providers, knowing that the creditor would be forced to absorb such increases in costs even though they have no legitimate basis. The CFPB's proposed requirement would increase costs for creditors. As a result, creditors would be forced to pass such increased costs onto consumers in the form of higher origination charges.

It is our understanding that HUD interpreted the analogous tolerance regime under Regulation X differently with respect to the written list of providers. HUD interpreted the failure to provide the written list of providers that was required under Appendix C of Regulation X as substantively similar to the creditor listing all available providers on the written list of providers. This meant that charges for which the consumer could shop for the provider would fall in the 10% tolerance category regardless of the provider selected by the consumer. The KBYO rule currently mirrors HUD's approach, which we believe provides continuity for the industry in an ever-changing regulatory environment.

In short, The CFPB's proposal would change a framework that has been in place for almost a decade. The Associations believe that because of the potential increased cost to industry of such a change, as well as the potential harm to consumers from creditors passing such increased costs onto consumers, the CFPB should conduct a more robust analysis of the costs and impacts of such a change before finalizing this aspect of the rule.

Construction Lending: New comment 17(c)(6)-6—Financing By Same Creditor

The proposed rule appears to set forth a new requirement in instances where a creditor receives a credit application for construction loans. The proposed comment 17(c)(6)-6 would appear to define "may be permanent financed by the same creditor" as used in § 1026.17(c)(6)(ii) to mean, "if the creditor generally makes both construction financing and permanent financing available to qualifying consumers, unless a consumer expressly states that the consumer will not obtain permanent financing from the creditor." The proposal would also add comment 19(e)(1)(iii)-5, which would attempt to clarify the timing requirement for the initial LE that applies to such transactions. This comment essentially states that a loan subject to § 1026.17(c)(6)(ii) requires an initial LE to be disclosed for both the construction and permanent phases upon application, even if it is for "construction financing only." The proposed comment provides an example under comment 19(e)(1)(iii)-5.i that states if a creditor receives an application for "construction financing only," it "must" provide the initial LE for both a construction and permanent loan within three business days of receipt of the application for "construction financing only." The only exception to the dual disclosure provision would be obtaining express statement that the consumer will not seek permanent financing from that creditor, as described under comment 17(c)(6)-6.

The Bureau described in the preamble language that it proposed comment 17(c)(6)-6 because, "at the early stages of an application when the Loan Estimate is delivered, creditors usually would not yet have made a determination as to whether they will provide permanent financing to any given consumer," and a determination when they decide they will "could be complex." Further, the Bureau stated that it "does not believe it is appropriate to determine whether a creditor 'may' provide permanent financing based on the creditor's actual determination as to any individual consumer."

For various reasons, we oppose this new requirement. Adding this dual disclosure requirement would confuse consumers, complicate compliance for lenders, create internal conflict with other portions of the rule, and quite possibly, be unauthorized under the TILA and RESPA statutes. Our thinking is set forth below.

- *Unnecessary:* The Associations believe that the CFPB's stated reasoning for these proposed provisions is unfounded. The CFPB stated that it is difficult for creditors to determine when a loan may be permanently financed under the current provisions, and that it is inappropriate to determine whether a creditor may provide permanent financing based on the creditor's actual determination as to any individual consumer. But this is how Regulation Z currently works, and there does not appear to have been any particular confusion with respect to this issue. Specifically, for a "construction only" loan, the consumer has not yet applied for a permanent transaction (even if he or she has not expressly stated they would not obtain a permanent loan from the creditor), and thus, no determination about possibly permanently financing the construction loan needs to be made during the origination of this loan. Once the consumer actually decides to apply for permanent financing, the creditor would have a firm date on which to base its timing requirement for the initial LE.

- *Consumer Confusion:* As a threshold matter, the Associations believe that giving consumers a disclosure for a financial product they are not seeking will overwhelm them and quite possibly confuse their comparison analysis. The receipt of two loan disclosure packets will baffle a consumer that only asked for construction-related financing, and will undoubtedly lead a shopper to misunderstand which packet applies to the particular type of loan on which they are focused. Consumers will not understand the rule enough to expressly state that they do not want construction financing to avoid the duplicative paperwork. This will likely lead to excessive paperwork being provided to consumers for a loan they did not apply for, because most banks will want to treat the construction phase separately in their software systems to be able to move forward with that transaction only, because that is the loan for which the consumer "actually" applied. As a result, the bank's system would provide a separate disclosure package for a loan for which the consumer did not apply, burying the consumer in unnecessary paperwork during a critical time in their decision-making process. A key goal of the KBYO initiative, as well as the CFPB's efforts to simplify the closing process, is to reduce the bulk and to simplify credit disclosures; this proposal would achieve the exact opposite.

  Relatedly, we also think that this requirement will lead to customer distrust towards the bank. "Why," they will ask, "is my bank giving me disclosures for additional loans that I did not request?" Without doubt, the additional unrequested disclosure package will feel like a marketing and pressure tactic to induce the customer to purchase more products than what they asked for. Explaining to the consumer that government regulations require such additional disclosures rarely eases the apprehension and coercion that customers sense towards banks that appear to overwhelm them with bank-related products. In this sense, and from the perspective of consumer expectation, the CFPB's provision gets this completely reversed—the only time a lender should be obligated to provide permanent financing disclosures is when the consumer expressly indicates they desire a particular product (here, the permanent financing) from that lender.

In addition, banks may attempt to shield their customers from the unnecessary paper using various methods. Some banks may add an explanatory disclosure to the disclosure package for the permanent loan for which the consumer did not apply for, to explain why the second batch of disclosures is being provided. Other banks may be forced to require the consumer to sign an additional document that affirms the consumer does not want an additional financial product before they actually accept any application information—to avoid a potential violation of the timing requirements for the initial LE, which cannot be cured under the rule. These approaches do not appear optimal, and the additional disclosures will just add to the paperwork that consumers receive as they wade through the application and origination process, also adding to the risk of "information overload."

- *Consumer Harm and Legal Complications from Inaccurate Loan Estimates for an Inchoate Permanent Loan:* Consumers who have only applied for construction financing may be harmed because the disclosures for the permanent loan may be at such an early stage that banks will not be able to provide accurate pricing disclosures for the permanent loan. At an early stage, consumers only interested in construction financing may not have provided sufficient information or documentation with respect to the permanent financing. In addition, many of the third party vendors involved in the settlement process will not have been identified, such that the accuracy of the cost estimates will suffer. Consumers may make financial decisions based on this early disclosure for the permanent phase for which they did not apply, which may not be the most accurate information.

  Further, there are legal complications to offering a Loan Estimate that carries legal liabilities and price guarantees under the tolerance requirements. A consumer who has not applied for the permanent loan product may not have the information or documentation necessary to provide accurate pricing disclosures. Although there may be the ability to revise estimates under § 1026.19(e)(3)(iv), the estimates are still subject to the "good faith standard," which requires creditors to conduct "due diligence" to obtain the best information reasonably available. See comment 19(e)(1)(i)-1. This burden is made more difficult, and the legal risk that much greater, at this early stage. In addition, the credit and underwriting decisions necessary for a one or two-year construction loan differ substantially from considerations required for a 30-year loan. The former is likely to be held in portfolio and managed by bank experts that understand how to manage its procedures. The latter is likely to be sold to secondary market players and therefore require completely different staff, third party relationships and back office coordination. In fact, the form production, compliance and underwriting systems for each of these types of loans will likely be different, and they cannot necessarily be ignited in tandem to achieve simultaneous assembly and delivery to the customer. Importantly, we note that the laws that apply to each type of loan differ widely. Suffice it to note that construction loans are not covered by the ability-to-repay rules that generate a full body of compliance procedures that do not apply to other types of transactions.

- *Legal Questions Regarding the Proposed Provisions:* In addition, this proposal is too muddled, complex, and extremely confusing for purposes of compliance. The full scope of the requirement can only be ascertained by reading through four separate, interlocking provisions and examples. Our seasoned compliance and outside legal experts struggled in assembling its various parts. We respectfully submit that there are inconsistencies with this proposal and existing regulatory provisions. We note, as a general matter, that commentary provisions cannot override the regulatory text or create regulatory requirements. Commentary provisions only provide safe harbors of compliance for following the regulatory text. See App. C of Reg Z, and the introductory comment I—1. It is therefore important that the regulatory language be fully consistent.

  Section 1026.17(c)(6)(ii) states that when a construction loan "may be permanently financed by the same creditor," it can be treated as either one or more than one transaction. The regulatory text of § 1026.17(c)(6)(ii) contemplates such a transaction being one evidenced by one loan. Specifically, this regulatory text refers to the construction and permanent "phases" of one, singular "loan" to be disclosed as combined or separate transactions. The regulatory text does not provide an option to disclose a separate "permanent loan" combined with a separate "construction loan." This interpretation is confirmed by the existing commentary. Specifically, existing comment 17(c)(6)-2 already describes when this option under § 1026.17(c)(6)(ii) is available, which describes such transactions that "may be permanently financed" as when, "unless the obligation is paid at that time, the loan then converts to permanent financing in which the loan amount is amortized just as in a standard mortgage transaction." This "converts" word appears to assume that this conversion is built into the terms of one legal obligation. Most legal experts have assumed that this terminology has always meant that it did not apply to true separate "construction only" loans that do not have some conversion built into the note or other terms of the legal obligation. Most legal experts have assumed that Regulation Z has treated "construction only" transactions as separate transactions, meaning a subsequent permanent transaction has to be treated separately under Regulation Z. This interpretation conforms to the differences between the terms of the legal obligation between construction-to-permanent financing and construction-only loans. A transaction that is a construction-only loan would only include a promissory note for the construction financing, and would not contain any terms that contemplated a conversion to permanent financing. In contrast, many construction-to-permanent transactions include a promissory note for the permanent phase and a rider for the construction phase that is executed at one closing at the beginning of the construction phase, but which note may be modified in a separate closing at the end of the construction phase.

  Based on this analysis, most legal experts interpret the regulatory text and existing comment 17(c)(6)-2, which the CFPB has not proposed to amend or delete, to mean that

> truly separate construction and permanent transactions should be treated under Regulation Z as separate transactions.
>
> However, in spite of this regulatory text and the existing interpretation in the commentary, which would remain in the rule, the CFPB appears to have attempted to create a new conflicting legal requirement that applies to applications for "construction financing only" in proposed comment 19(e)(1)(iii)-5.i. This commentary provision would use the word "must" and require a disclosure for an application for a permanent loan that has not yet been submitted by the consumer. This appears to conflict with § 1026.17(c)(6)(ii) and existing comment 17(c)(6)-2, as well as the general tenets of Regulation Z. As stated above, the commentary cannot create regulatory requirements, and it should not conflict with existing commentary. Therefore, we believe this proposed commentary will complicate compliance, rather than provide greater clarity and certainty.

In summary, this precise requirement should be removed from any final rule. The Bureau specifically sought comments on an alternative approach that would allow a creditor to provide the Loan Estimate only for the financing for which the consumer applied. The associations would support this option. Under the approach described by the proposal, if a consumer applied for construction financing only, a creditor would be required to provide the Loan Estimate for only the construction financing. If the construction financing may be permanently financed by the same creditor, the creditor would be permitted to provide the Loan Estimate for the permanent financing at the same time as the Loan Estimate was provided for the construction financing, but would not be required to do so. If the consumer applied for construction and permanent financing at the same time, the creditor would be required to provide the Loan Estimates for both phases within three days of receiving the application. If the consumer applied for construction and permanent financing separately, the creditor would be required to provide Loan Estimates within three days of receipt for each application. However, a Loan Estimate for the separately-applied-for permanent phase would not be required if the Loan Estimate for the permanent phase had already been provided because the transaction met the condition that the construction phase may be permanently financed by the same creditor.

Payoffs and Construction Costs as ''Other'' Costs

Proposed comment app. D–7.vii.A would explain the amount of construction costs is disclosed under the subheading ''H. Other'' on the standard disclosure under § 1026.37(g)(4), consistent with informal guidance provided by the Bureau and the proposed changes to the commentary to § 1026.37(g)(4) (and their analogous provisions for the CD). Such costs would be disclosed under Payoffs and Payments on the alternative disclosure for transactions without sellers. In addition, the CFPB proposed to amend the commentary to §§ 1026.37(g)(4) and 1026.38(g)(4) to provide that other payoffs, such as payoffs of prior liens in refinance transactions, or payoffs of unsecured debt, would be required to be disclosed under "H. Other" on the standard disclosure, but under Payoffs and Payments on the alternative disclosure for transactions without sellers.

Although verbal webinar guidance by the Bureau had allowed creditors an alternative option for disclosing construction costs in the Calculating Cash to Close table (not as "Other" costs), the Bureau is now proposing a more definitive rule where creditors would be required to disclose construction costs under "H. Other."

The Associations appreciate the proposal's aim to provide clarity and precise instruction regarding the disclosure of construction costs. However, the Associations note, below, several considerations regarding this proposed disclosure placement. The Associations suggest that the Bureau should instead require disclosure of payoffs and construction costs as payoffs in the Summaries of Transactions, and in the Adjustments and Other Credits row of the "calculating-cash-to-close" table. This would ensure that closing costs appear together on the forms, but separate from payoffs and construction costs, which consumers do not think of as closing costs.

In support of this alternative, the Associations note several considerations regarding this proposed disclosure placement:

- Our bankers observe that if the "H. Other" section were to contain various types of pay-offs—for instance, unsecured credit card debt, payoffs of prior mortgage liens, etc., that could swell this amount and the total closing costs substantially (if a creditor chooses the standard disclosure for a Refinance construction loan, this box would contain the pay-off of the prior mortgage as well as construction costs). In short, the proposal will result in making the closing costs in many loans, including construction loans, appear to be enormous. This large number will cause concern and confusion on the part of consumers.

- The disclosure approach set forth by the proposal may cause operational difficulties due to the Bureau's decision to vary the disclosure methodology between the standard and the alternative forms. The apparent result under the proposed rule is that creditors would be required to list payoffs and construction holdbacks under Payoffs and Payments on the alternative disclosures, but when using the standard disclosures, creditors would list them in the "H. Other" section. This would require creditors to input these costs into their systems differently, depending on which version of the disclosures they were using, which will create software and staff training difficulties. In addition, this dichotomy is confusing to consumers, especially consumers comparing loans between creditors using the different versions of the disclosures. We also note that proposed comment app. D–7.vii.A does not expressly refer to the alternative disclosure, which is only referenced in the proposed commentary to 1026.37(g)(4), which creates legal complexity and may introduce different interpretations between creditors and investors, causing confusion for the industry.

- The proposed disclosure approach is likely to cause problems with systems software. We note that compliance systems will have to be tweaked to recognize the position of the payoffs and construction cost information, depending on the version of the disclosures used, in order to properly process it under other provisions and requirements. In addition, the systems software uses this information for underwriting and qualification of the consumer, which potentially includes interaction with automated underwriting systems. This will need to be modified to properly process this different placement of the construction cost information. Further, many different software systems may be involved in the origination of a loan and the production of the disclosures, including loan origination software, lender's document production software, title production software, as well as collaborative closing portals. All of these software systems may program this disparate set of payoffs and construction costs between the standard and alternative disclosures differently. Some systems may require coding of such costs only as payoffs and then automatically place the data differently between the versions of the disclosure, while some may require the user to code such costs differently as payoffs or closing costs between the different forms. The difference in data formats may increase costs and frustrate the industry's efforts to utilize uniform data standards.

A Better Approach on Construction Financing

Over the past several months, bankers have reported acute difficulties in complying with the KBYO construction lending rules. Numerous bankers have determined that construction and construction-to-permanent financing is unfeasible due to uncertainties in compliance. Our bankers that engage in construction lending report that KBYO's computation flows are convoluted and the numerical outcomes, such as the Cash to Close, are inconsistent with actual amounts. There is also lingering confusion with many individual provisions of the rule, including disbursements of construction contract costs, the projected payments table, individual disclosures for adjustable rates, and variations applicable to the alternative disclosures, among other issues. The Associations observe that the ongoing regulatory disarray has sparked a flight away from construction financing by many banks. Our members have reported significant levels of abandonment of this segment, and those that remain do so precariously, without any assurance that their loans will be safe from future penalties or even litigation.

We also note that, for various reasons, high levels of confusion and indeterminate risk will remain even after any clarifications under this proposal are finalized. In addition to lack of regulatory clarity, construction lending is not a commoditized transaction, and their precise terms and/or structures vary greatly. Construction loans may be for initial construction (building the home where the borrower will reside) or subsequent construction (such as rehabilitation or remodeling). Construction periods usually involve several disbursements of funds at disparate times throughout the project, some of which may include differing amounts of fees for requisite inspections. Transactions also differ as to conversions, where some provide that the obligation is paid at the conclusion of construction, and others provide for a conversion into permanent financing. On top of all these variations, there are local laws and requirements that add to disparities in financing arrangements and methodologies. All of these variants result in a loan product that does not conform well to the extremely detailed and rigid disclosure structure of KBYO.

More important, however, are observations that the current disclosure methodology for construction-only and construction phases of construction-to-permanent loans under KBYO may actually harm consumers. It has been reported by our members that their applicants and borrowers are confused by much of the information on the KBYO disclosures, such as the projected payments table and loan terms table. For example, the rules for the loan terms and projected payments tables do not require disclosure of the maximum interest payment that may be due during the construction phase, in part, because of the assumptions under appendix D of Regulation Z. While the Bureau determined that it was important for consumers to understand their maximum possible payment for regular permanent financing, the KBYO rule was not designed to provide this important information to consumers for construction-only loans or their construction phases of construction-to-permanent loans. Further, it is extremely difficult to determine how to disclose the frequency of adjustments of adjustable rates under KBYO for these transactions.

In the end, we offer that construction loans are, in essence, loans for the purchase of *construction services*, while the KBYO disclosure regime is tailored towards loans for real estate purchases or refinances. This incongruity forces a situation where construction and construction-to-permanent financing, like reverse mortgages and home equity lines of credit, would be best separated out of the KBYO regulations. The CFPB has wisely decided to exclude reverse mortgage loans from KBYO and address them in a separate, future rulemaking because it determined that applying the KBYO requirements to such loans would, "would likely result in confusion for consumers and industry."[5] The CFPB came to a similar conclusion for home equity lines of credit, stating that subjecting them to KBYO, "would likely result in confusion because many parts of the disclosures would be inapplicable to open-end credit transactions."[6] We believe that, based on facts described above, these conclusions apply to construction and the construction phase of construction-to-permanent transactions as well.

The Associations urge that temporary financing transactions that generally encompass construction lending be excluded from KBYO coverage. We respectfully submit that if the Bureau intends to cover and regulate all the divergent aspects of construction financing that exist across all communities, it will needlessly entangle itself in regulatory quagmires. Bureau instruction will result in endless detail and variation, requiring the Bureau to provide continuous and substantial amounts of informal guidance and formal updates to the KBYO rule.

We urge the Bureau to enact an exclusion from KBYO for temporary financing covering construction-only loans and the construction phase of a construction-to-permanent loan (and the associated fees and escrow arrangements). Under this approach, pure construction loans would not be covered by KBYO, and only the permanent phase of a construction-to-permanent loan would be subject to the KBYO requirements. The Bureau could immediately initiate more study into consumer patterns and shopping behavior in construction and construction-to-permanent transactions.

We offer the following observations on our recommendations:

- The total exclusion of construction financing is the current rule under TILA's "Ability to Repay" rules, where there is an exemption for construction, temporary or "bridge" loans with a term of 12 months or less. To date, there is no indication that those exempted transactions are subject to increased abuse, or that consumers have suffered due to its exempted status.
- Construction-to-Permanent loans are generally structured as two distinct phases. Since the second, or permanent phase, of the transaction will be fully subject to KBYO disclosures, the consumer will be well protected on the long-term financing of the overall project. The initial, or pure "construction" phase, which concerns contractor

[5] 78 Fed. Reg. at 79794.

[6] 78 Fed. Reg. at 79795.

negotiations, disparate disbursements of funds at times and in amounts that are unascertainable at the start, and interest-only payments to the lender by the consumer, is really about project management, and not about financing. The Bureau should focus on assuring viability and consumer safety with regard to the long-term *financing* of the deal, and should not ensnare itself with supervising and disentangling the myriad arrangements consumers have with their general contractors.

- A temporary exclusion would afford a respite that would allow the Bureau additional time to better study and analyze the disclosure methodology for these transactions. During this exemption period, the regulations could allow for the optional use of the existing KBYO instructions regarding construction loans, or alternatively, the old TILA and RESPA disclosures, as per previous Regulation Z and X rules and instructions. Again, this exemption would apply only to construction-only loans and the construction phase of a construction-to-permanent loan. Most importantly, a final product would be created with the input of banks and lenders that actually provide construction financing, to ensure the product addresses as many variances as possible, to ensure it would not hinder needed credit flows to home construction projects or consumer understanding.

It is clear that construction financing is a very valuable financial product in many regions of the country. For example, construction financing has been important to the recovery of areas affected by recent severe weather events, such as Hurricanes Sandy and Matthew. It is also clear that the ambiguities under KBYO are currently impeding access to the availability of these programs. We urge that the Bureau recognize this untenable state of affairs, and that it take affirmative steps to alleviate the ongoing confusion. The Associations believe our recommendation would result in gains for consumers, industry, the Bureau, and all communities that depend on this type of financing for growth and economic development.

Conclusion

The Associations appreciate the Bureau's continued focus on the mortgage disclosure rules, and we appreciate the opportunity to comment on these proposed amendments to the KBYO regulations. The Associations look forward to working with CFPB staff as it advances in this rulemaking. Please contact the undersigned if you have any questions regarding the Associations' comments on the proposal.

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